No. 12,559

IN THE

United States Court of Appeals

For the Ninth Circuit

MOORE EQUIPMENT CO., INC. (a corporation),

Appellant,

vs.

JOHN O. ENGLAND, as Trustee of the Estate of Ted E. Fisher and Maxine R. Fisher, Bankrupt,

Appellee.

Appeal from the United States District Court, Northern District of California, Northern Division.

APPELLANT'S OPENING BRIEF.

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STATEMENT OF FACTS.

The facts are undisputed and were stipulated to by the parties in District Court.

On May 25, 1948, Ted E. Fisher, hereinafter referred to as the Bankrupt, and Maxine R. Fisher, his wife, filed their voluntary petition in bankruptcy. Thereafter, John O. England was appointed trustee.

Prior to filing his petition and on February 26, 1948, the Bankrupt purchased from Moore Equipment

Co., Inc., a California corporation, maintaining its principal place of business in San Joaquin County, an Allis-Chalmers WC road grader. The Bankrupt executed a promissory note in the sum of $14,965.68 in payment of the full purchase price of the grader and in part payment of other equipment, not material herein. The note was payable in installments at the rate of $3,000.00 on April 1, 1948 and $997.14 per month on the first day of each month thereafter for twelve successive months. As security for the payment of this note, the Bankrupt made and executed a chattel mortgage to the corporation on the road grader and other equipment.

The chattel mortgage provided in part that the mortgaged equipment was to be permanently located and garaged in Mantecta, San Joaquin County, California, and provided further that the Bankrupt resided at that place. The Mortgage was recorded in the office of the County Recorder in and for San Joaquin County on February 28, 1948.

After the execution of the chattel mortgage and more than thirty days prior to April 8, 1948, the Bankrupt voluntarily removed the mortgaged property from San Joaquin County, California, to Stanislaus County, California. The property remained in Stanislaus County more than thirty days after the removal.

On April 8, 1948, defendant repossessed the road grader in Stanislaus County. At the time of repossession, the Bankrupt was in default in payment of the installment due and payable by the terms of the note.

After taking possession, and by virtue of the power of sale contained in said chattel mortgage, and in accordance therewith, Moore Equipment Co. sold the grader at private sale on May 1, 1948, to a bona fide purchaser for value. The chattel mortgage was not recorded in Stanislaus County at any time. The property was not disposed of as a pledge.

The value of the property at the time of sale was the sum of $1,860.

The District Court held that appellant obtained a preference under Section 60B of the Bankruptcy Act when it repossessed the grader under Section 2965 of the Civil Code of the State of California, because it did not dispose of the grader as a pledge pursuant to Section 2966 of the Civil Code of the State of California.

SPECIFICATIONS OF ERROR IN FINDINGS OF FACT AND CONCLUSIONS OF LAW.

Findings of fact numbered 10, 11, 12 and 13 are specified as error. These findings are alleged to be erroneous by reason of the fact that the same are conclusions of law, inconsistent with the facts stipulated by the parties.

Conclusions of law numbered 1, 2, 3 and 4 are specified as error for the reason that the same are unsupported by the facts stipulated to by the parties and found by the Court.

PRELIMINARY ANALYSIS.

This case involves the right of a mortgagee under a purchase money mortgage to repossess non-automotive personal property when the property has been removed from the county in which the mortgagor resided and the property was situated at the time of the delivery of the purchase money mortgage. There is a square conflict in the decisions as to whether or not a preference ever results where the mortgagee repossesses prior to actual bankruptcy, even where the mortgage is void for lack of compliance with state statute. Under the Massachusetts rule,[1] a mortgagee under a mortgage void for lack of recording may repossess prior to bankruptcy without effecting a preference, on the theory that the mortgage is valid between the parties. Under the New York rule, the mortgagee does not validate an invalid lien by the mere act of taking possession.[2] California follows the New York rule. Thus, a mortgagee does not acquire any rights by taking possession where a mortgage is void for lack of due execution, failure to record or delay in recording.[3]

In instant case, we are dealing with a mortgage which created a valid lien and the mortgaged property

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[1] *Mason v. Wylde,* 308 Mass. 268, 32 N.E. (2d) 615; certiorari denied, 62 Supreme Court 74, 314 U.S. 638;
American Nat. Bank v. Harris (Okla.), 84 F. (2d) 181, 31 A.B.R. (N.S.) 417.

[2] *Stephens v. Perrine,* 143 N.Y. 476, 39 N.E. 11.

[3] *Noyes v. Bank of Italy,* 206 Cal. 266, 274 P. 268;
Chelhar v. Acme Garage, 18 C. A. (2d) (Sup.) 775, 61 P. (2d) 1232;
Bank v. Sampsell, 114 F. (2d) 211.

was thereafter removed to another county. The facts being undisputed, a single question of law is presented for determination. Did appellant re-establish a pre-existing valid lien by taking possession of the mortgaged property pursuant to Sections 2965 and 2966 of the Civil Code of the State of California? If in fact the lien was re-established, appellant was a secured creditor with a paramount lien and no preference could result.

ARGUMENT.

I.

APPELLANT'S CHATTEL MORTGAGE, PRIOR TO THE REMOVAL OF THE MORTGAGED PROPERTY TO ANOTHER COUNTY, WAS A VALID SUBSISTING LIEN AGAINST THE MORTGAGED EQUIPMENT.

No claim is made by the trustee that the chattel mortgage was not executed and recorded in accordance with Section 2957 of the Civil Code of the State of California. It was recorded in the County of San Joaquin on the second day after its execution. The mortgagor resided in that county and the mortgaged equipment was located there. There is no element of lack due to execution, failure to record or delay in recording. Upon compliance with the statute, appellant acquired a property right in the mortgaged equipment good against all creditors of the mortgagor.

II.

THE REMOVAL BY THE MORTGAGOR OF THE MORTGAGED PROPERTY, AND ITS LOCATION IN THE COUNTY OF REMOVAL FOR MORE THAN THIRTY DAYS SUSPENDED THE PRE-EXISTING VALID LIEN.

The pertinent statutes relating to removal of mortgaged property are Sections 2965[4] and 2966[5] of the Civil Code of California. These statutes furnish the legislative solution to the problem of removal of mortgaged property in California. A majority of states require no additional action on the part of the mortgagee to preserve his lien. Other states, like California, require the mortgagee to follow the property and protect the lien by an additional filing.[6]

Under Section 2965 of the Civil Code the lien on the mortgage is not affected for thirty days after the

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[4]See. 2965. (Mortgaged personal property, effect of removal.) When personal property mortgaged (other than animate personal property mortgaged by a resident of this state, and motor vehicles and other vehicles defined in and the mortgaging of which are regulated by the California Vehicle Act), is removed from the county in which it is situated, the lien of the mortgage shall not be affected thereby for thirty days, after such removal; but, after the expiration of such thirty days, said property mortgaged, is exempted from the operation of the mortgage, except as between the parties thereto, until either:

1. The mortgagee causes the mortgage to be recorded in the county to which the property has been removed; or

2. The mortgagee takes possession of the property as prescribed in the next section.

[5]Sec. 2966. (Mortgagee may take possession and sell property as pledge, when.) If the mortgagor voluntarily removes or permits the removal of the mortgaged property save in the case of animate chattels mortgaged by a resident of this state, from the county in which it was situated, at the time it was mortgaged, the mortgagee may take possession and dispose of the property as a pledge for the payment of the debt, though the debt is not due.

[6]For cases in other jurisdictions see: Jones—Chattel Mortgages and Conditional Sales, Par. 260, Vol. 1, page 434. See also: 103 A.L.R. 198, Annotation—Chattel Mortgage—Removed Property.

removal of the mortgaged property.[7] After the expiration of such thirty days, the property "is exempted from the operation of the mortgage except as between the parties thereto until either (1) the mortgagee causes the mortgage to be recorded in the county to which the property has been removed or (2) the mortgagee takes possession of the property as prescribed in Section 2966."[8]

The pertinent portion of Section 2965 was incorporated into the law in 1909.[9] Its present form was the result of amendments in 1923 and 1935 to cover matters not here material.[10] Prior to the 1909 amendment, the statute provided that the property was "exempted from the operation thereof unless either" the mortgagee within thirty days after such removal recorded in the new county or within thirty days took possession of the property.[11] In *Hopper v. Keys*[12] the early statute was interpreted to mean that failure by the mortgagee to record in the new county or take possession of the property removed before thirty days had elapsed exempted the property for all time from the mortgage lien; that it voided the mortgage and no subsequent recordation or taking of possession could revive it. Under the present statute, the lien is not voided for all time but merely suspended until such time as the mortgagee shall take affirmative action. The statutory words "exempt from the operation of

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[7]*Pacific Fruit Exchange v. Booth Co.*, 103 C. A. 54, 283 P. 944.
[8]Notes 4 and 5, supra.
[9]Statutes 1909, page 44.
[10]Statutes 1923, page 139; Statutes 1935, page 2227.
[11]Enacted March 21, 1872.
[12]152 Cal. 488, 92 Pac. 1017.

the mortgage" express a clear legislative intent that the mortgage is not void but is voidable only until the mortgagee records or takes possession.[13]

III.

THE PRE-EXISTING VALID LIEN WAS RE-ESTABLISHED BY THE MORTGAGEE TAKING POSSESSION.

The argument here covers a pivotal point in this case. Is the lien re-established by the mortgagee's affirmative act in re-possessing the property, or is the "exemption from the operation of the mortgage" removed only by re-possession plus sale as a pledge? We find no cases construing these statutes.

The answer to this question obviously involves the construction of Sections 2965 and 2966.[14]

It is noted that by its terms Section 2965 requires only that the mortgagee *take possession of the property* as prescribed in the next section. It does not require that the mortgagee take possession *and sell* as prescribed in the next section. To adopt the trial Court's construction of the statute is to place into the statute words that the statute does not contain. If the trial Court's construction were adopted the statute would read:

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[13]See *California Law Review*, Vol. 16, pages 135, 137:
"In other words, under the amended section, the lien is not voided for all time, but merely suspended until such time as the mortgagee shall act."

[14]Notes 4 and 5, supra, for text.

> "2. The mortgagee takes possession of the property *and sells* as prescribed in the next section."

It is submitted that this construction is strained and unwarranted in view of the fact that the mortgagee has acquired a property right by the initial recording of his chattel mortgage.

It would appear that 2965 and 2966 can be read together without conflict giving full effect to all of the words of both statutes. Section 2966 accomplishes two things:

> (1) It authorizes the mortgagee to take possession and thus remove the exemption of 2965; and
>
> (2) It implements the possession thus obtained with a power to sell as a pledge even though the debt is not due.

It thus provides the necessary relief to a mortgagee whose property has been surreptitiously removed but whose debt is not due. The statute, in effect, provides for a statutory acceleration of the maturity of the debt once possession is taken. Otherwise, the mortgagee could take possession, but the debt not being due, could not foreclose. Only this interpretation gives full effect to the use of the words "though the debt is not due" in the statute.

In the instant case, the debt was due and the mortgagee foreclosed under the power of sale contained in the mortgage. Appellant did not have to avail itself

of the statutory authorization to sell as a pledge because the debt was due.

Traditionally, taking possession of mortgaged property and the sale thereof are separate acts. The mortgagee's power of sale is determined by the statutes or by the terms of the mortgage instrument in accordance with rights given to him by the mortgagor. California permits liberal use of the power of sale contained in a mortgage.[15] It is submitted that it is a strained construction of the statute to say that in all other cases a mortgagee may exercise a power of sale conferred by a mortgage, but if he repossesses property wrongly removed from the county in which it is located he must then disregard the terms of his mortgage and dispose of the property as a pledge. To so hold would enable a mortgagor to enlarge his rights by tortious and wrongful conduct.

A further logical difficulty is encountered in adopting the trial Court's construction of the statute. The Court holds that the lien is re-established only by a sale as a pledge. However, a sale does not create a lien—it extinguishes the lien. It is therefore logically inconsistent to construe a statute so that a lien is re-created only by an act of sale which extinguishes it.

The trial Court's strained construction of Section 2966, if adopted, is fraught with further difficulties. If the lien is revived only by repossession plus sale

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[15]*Dohrman v. Durstow*, 90 C. A. (2d) 236, 202 P. (2d) 607. Agreement for informal foreclosure at private sale, with or without notice is valid.

as pledge, it would follow that after possession and prior to a sale a judgment creditor could levy on the property. This would be contrary to the provision of Section 2965, which states that the mortgaged property is exempted only until "the mortgagee takes possession."

CONCLUSION.

It is submitted that a reasonable construction of the statutes reflects the legislative intent that the exemption from the operation of the mortgage should continue only until the mortgagee takes affirmative action either by recording in the new county or by taking posession; and that Section 2966 merely implements the mortgagee's possession by giving a power to sell though the debt is not due. The equities in this situation wholly favor appellant. Appellant properly recorded its mortgage in San Joaquin County and when it ascertained that the property had been removed it repossessed it. Since the debt was then due, it sold the property to a bona fide third person under the power of sale contained in the mortgage. The Bankrupt paid nothing for the property and had the full use of it prior to repossession. The creditors were in exactly the same position after the repossession as they were before the personal property was sold to the Bankrupt. To say that a mortgagee must dispose of the property as a pledge when the debt is already due takes from such mortgagee a substantial right guaranteed to him by the contract between the parties.

Such a construction of the statute should not be made when it can be given an obvious construction consistent with the rights of the parties.

Dated, Stockton, California,
August 4, 1950.

Respectfully submitted,
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